



6712-01

FEDERAL COMMUNICATIONS COMMISSION

47 CFR Part 64

[CC Docket No. 00-175, FCC 13-69]

2000 Biennial Regulatory Review, Separate Affiliate Requirements of the Commission's Rules

AGENCY: Federal Communications Commission.

ACTION: Notice of proposed rulemaking.

SUMMARY: In this document, the Commission seeks comment on the structural separation requirements of the Commission's rules, as they apply to rate-of-return carriers providing facilities-based in-region, interexchange, interstate long distance services. Specifically, the Commission seeks comment on the costs and benefits of continuing to apply requirements to rate-of-return carriers, and whether such carriers continue to have the ability and incentive to engage in anticompetitive behavior.

DATES: Comments are due on or before **[INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]** and reply comments are due on or before **[INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

ADDRESSES: Interested parties may submit comments, identified by CC Docket No. 00-175, by any of the following methods:

- Federal eRulemaking Portal: [http:// www.regulations.gov](http://www.regulations.gov). Follow the instructions for submitting comments.
- Federal Communications Commission's Web site: <http://fjallfoss.fcc.gov/ecfs2/>. Follow the instructions for submitting comments.

- People with Disabilities: Contact the FCC to request reasonable accommodations (accessible format documents, sign language interpreters, CART, etc.) by email: FCC504@fcc.gov or phone: (202) 418–0530 or TTY: (202) 418–0432.

For detailed instructions for submitting comments and additional information on the rulemaking process, see the **SUPPLEMENTARY INFORMATION** section of this document.

FOR FURTHER INFORMATION CONTACT: Gregory Kwan, Attorney Advisor, at 202-418-1191, Competition Policy Division, Wireline Competition Bureau.

SUPPLEMENTARY INFORMATION: This is a summary of the Commission’s Second Notice of Proposed Rulemaking (Second FNPRM) in CC Docket No. 00-175, released on May 17, 2013. The full text of this document, which is part of the Commission’s Memorandum Opinion and Order and Report and Order and Further Notice of Proposed Rulemaking and Second Further Notice of Proposed Rulemaking, is available for public inspection during regular business hours in the FCC Reference Center, Room CY-A257, 445 12th Street, SW., Washington, DC 20554, and may also be purchased from the Commission’s copy contractor, BCPI, Inc., Portals II, 445 Twelfth Street, SW., Room CY–B402, Washington, DC 20554. Customers may contact BCPI, Inc. via their Web site, <http://www.bcpi.com>, or call 1–800–378–3160. This document is available in alternative formats (computer diskette, large print, audio record, and Braille). Persons with disabilities who need documents in these formats may contact the FCC by e-mail: FCC504@fcc.gov or phone: 202–418–0530 or TTY: 202–418–0432.

Pursuant to sections 1.415 and 1.419 of the Commission’s rules, 47 CFR 1.415, 1.419, interested parties may file comments and reply comments on or before the dates indicated on the first page of this document. All pleadings are to reference CC Docket No. 00-175. Comments may be filed using the Commission’s Electronic Comment Filing System (ECFS). See Electronic Filing of Documents in Rulemaking Proceedings, 63 FR 24121 (1998).

- Electronic Filers: Comments may be filed electronically using the Internet by accessing the ECFS: <http://fjallfoss.fcc.gov/ecfs2/>.
- Paper Filers: Parties who choose to file by paper must file an original and one copy of each filing. If more than one docket or rulemaking number appears in the caption of this proceeding, filers must submit two additional copies for each additional docket or rulemaking number.
- Filings can be sent by hand or messenger delivery, by commercial overnight courier, or by first-class or overnight U.S. Postal Service mail. All filings must be addressed to the Commission's Secretary, Office of the Secretary, Federal Communications Commission.
- All hand-delivered or messenger-delivered paper filings for the Commission's Secretary must be delivered to FCC Headquarters at 445 12th St., SW, Room TW-A325, Washington, DC 20554. The filing hours are 8:00 a.m. to 7:00 p.m. All hand deliveries must be held together with rubber bands or fasteners. Any envelopes and boxes must be disposed of before entering the building.
- Commercial overnight mail (other than U.S. Postal Service Express Mail and Priority Mail) must be sent to 9300 East Hampton Drive, Capitol Heights, MD 20743.
- U.S. Postal Service first-class, Express, and Priority mail must be addressed to 445 12th Street, SW, Washington DC 20554.
- People with Disabilities: To request materials in accessible formats for people with disabilities (braille, large print, electronic files, audio format), send an e-mail

to fcc504@fcc.gov or call the Consumer & Governmental Affairs Bureau at 202-418-0530 (voice), 202-418-0432 (tty).

Synopsis of Second Further Notice of Proposed Rulemaking

1. In furtherance of our commitment to revisit rules that may be outmoded, ineffective, insufficient, or excessively burdensome, while continuing to promote competition and consumer protection consistent with the Act, we evaluate in this Second FNPRM the structural separation requirements of section 64.1903 of the Commission's rules, as they apply to rate-of-return carriers providing facilities-based in-region, interexchange, interstate long distance services (in-region long distance services). Through this proceeding, we intend to modernize our rules to reflect the competitive and marketplace realities for long distance service—at one time an expensive service, today one frequently offered on an unlimited basis by numerous facilities-based providers.

2. Section 64.1903, as written, requires independent ILECs providing long distance services using their own facilities to do so through a separate corporate subsidiary that does not jointly own transmission or switching equipment with the local exchange company. The Commission promulgated section 64.1903 against a regulatory backdrop in which local telephone service, interstate long distance, and intrastate long distance were distinct services, for which consumers often chose separate providers. Since the codification of section 64.1903 more than fifteen years ago, we have seen transformative marketplace and regulatory changes, calling into question whether the current rule is the least burdensome way to ensure that our goals of competition and consumer protection are met. The Commission has acknowledged these changes, and in 2007 granted relief to the Bell Operating Companies (BOCs) from a regulatory framework with similar structural separation requirements as section 64.1903.

3. Today, the Commission adopts the USTelecom Forbearance Order, which, among

other things, grants the request of the United States Telecom Association (USTelecom) for forbearance from section 64.1903 as it applies to price cap carriers that comply with certain conditions. Based on the record in that proceeding, however, the USTelecom Forbearance Order denies similar relief to independent ILECs subject to rate-of-return regulation “due to the continuing potential for cost misallocation.” In this Second FNPRM, we take the next steps toward modernizing our rules for the non-BOC ILECs. Considering developments in today’s marketplace, we seek comment on the costs and benefits of continuing to apply section 64.1903 to rate-of-return carriers, and whether such carriers continue to have the ability and incentive to engage in anticompetitive behavior.

4. The Commission adopted section 64.1903 based on the findings in the LEC Classification Order emphasizing the need to protect against the exercise of exclusionary market power by independent ILECs—the ability to raise rivals’ costs of providing competitive services, including the misallocation of costs (for example misallocating costs from nonregulated to regulated services), non-price discrimination (for example, lower quality wholesale services provided to a competitor), and a price squeeze based on inputs that long distance competitors need, such as access services (for example, raising prices for access services, including both switched and special access, or reducing prices for retail services). In light of the market changes described above, we consider whether the rule continues to offer benefits and whether the benefits justify the regulatory burdens and costs of compliance for rate-of-return ILECs. We also recognize that market conditions alone might justify eliminating the separate affiliate requirement, at least for some independent ILECs subject to rate-of-return regulation, and seek comment on the relevant market characteristics and how they should affect our evaluation of the continued need for the separate affiliate rule.

5. Analyzing Potential for Cost Miscalculation. The USTelecom Forbearance Order granted forbearance from section 64.1903 to independent ILECs subject to price cap regulation

but denied this relief to such carriers subject to rate-of-return regulation, including both independent ILECs subject to average schedules and cost companies. Rate-of-return regulation, which preceded price cap regulation, focuses on an ILEC's costs and fixes the profits an ILEC may earn based on those costs. A rate-of-return ILEC may recover only its costs plus a prescribed return on investment. Unlike price cap carriers, rate-of-return carriers are typically small, rural telephone companies concentrated in one area. Also unlike price cap carriers, non-average schedule rate-of-return independent ILEC has the ability and incentive to over allocate costs to common line and special access services because its interstate compensation for those services remains based directly on company-specific costs. We seek comment on this view. The Commission's 2011 reforms to intercarrier compensation rules cap and/or reduce interstate switched access charges, but allow increases in common line and special access rates. Thus, we believe that these changes in the access charge rules reduce, but may not eliminate, incentives for cost misallocation and potential access charge rate increases. We seek comment on this view and on the interplay between section 64.1903 and our intercarrier compensation and universal service reforms. We seek comment on whether we could address concerns about cost misallocation equally well, and in a less burdensome manner, in ways other than requiring that service be provided through a separate affiliate.

6. The Commission has previously recognized that concerns about cost misallocation are strongest when carriers provide long distance services in whole or in part through their own switching or transmission facilities. When these carriers provide long distance service exclusively through resale, the risk of cost misallocation is reduced, and they operate pursuant to a lesser safeguard—a separate corporate division rather than a separate subsidiary. We seek comment on the extent to which rate-of-return independent ILECs provide long distance service using their own facilities. Could we deter and detect cost misallocation by requiring that independent ILECs offering long distance over their own facilities provide those services through

a separate corporate division?

7. We also seek comment on whether we can reduce the burdens on average schedule carriers. Average schedule carriers are a subset of rate-of-return carriers that receive access compensation and universal service support through the use of “average schedules” to avoid the difficulties and expenses involved with conducting company-specific cost studies. Average schedule companies appear to have limited incentives to misallocate costs as long as they continue to use the average schedules for access compensation. However, these companies are permitted to convert to cost-based regulation without Commission approval. Thus, an average schedule company could, in theory, provide in-region long distance service without a separate affiliate, and then convert to cost-based regulation. We seek comment on how we could grant relief from the separate affiliate requirement for average schedule companies and also prevent them from misallocating costs in the future. We could condition relief from section 64.1903 on a commitment not to convert to rate-of-return regulation, or require them to reinstitute a separate affiliate if they do so. We seek comment on these and alternative suggestions. How should the Commission treat cost companies participating in NECA pools? Do these companies possess the ability and incentive to misallocate costs because disbursements from the NECA pools are based on participating companies’ costs? In the USTelecom Forbearance Order, we grant relief to price cap carriers if they: (1) submit and obtain Bureau approval of special access performance metrics, and (2) satisfy imputation requirements, including the submission of an imputation plan for review and approval from the Bureau. Will such nonstructural safeguards obviate the need for section 64.1903, while imposing fewer costs and burdens, for rate-of-return carriers? How should our analysis for rate-of-return carriers differ, if any, from our analysis for price cap carriers?

8. Analyzing Potential for Unlawful Non-Price Discrimination and Price Squeezes.

Section 64.1903 was intended to prevent unlawful non-price discrimination and price squeezes.

Do these concerns remain relevant in light of changes in the market, including the prevalence of bundled local, intrastate long distance, and interstate long distance services? Is the separate affiliate requirement an effective, cost-effective way to prevent these anticompetitive practices? Could the Commission effectively address these concerns through ex-post facto investigations, such as under a section 208 complaint process? Are existing statutory and regulatory safeguards sufficient to deter these anticompetitive practices?

9. Costs and Benefits of the Separate Affiliate Requirements of Section 64.1903. How many independent ILECs use separate affiliates pursuant to section 64.1903? What costs, if any, would be saved if we eliminate section 64.1903 for independent ILECs subject to rate-of-return regulation? Would the same savings be realized if the independent ILEC were required instead to provide long distance services through a separate division? For example, what incremental costs does an independent ILEC incur in maintaining separate books of account for its long distance services, as opposed to including those costs and revenues in the accounts for its ILEC operations? How does that differ depending on whether the separate books of account are for a separate division versus a separate corporation? We particularly seek empirical data on costs and burdens from independent ILECs that have experience providing long distance service through a separate corporate affiliate or a separate division so that we can analyze the differences between these structures.

10. What effect, if any, does the prohibition against joint ownership of switching and transmission equipment have on an independent ILEC's operational efficiency and ability to offer innovative services? Does that prohibition significantly limit the independent ILEC's opportunities to take advantage of economies of scope and scale associated with integrated operations? Does the prohibition make it more difficult for an independent ILEC to transform its network from a traditional Time-Division Multiplexing (TDM) network to an all-Internet Protocol (all IP) network? If so, how? Does section 64.1903 reduce independent ILECs' ability

to increase telephone subscribership or extend broadband services to additional areas? If ILECs transition to offering only VoIP services, should section 64.1903 continue to apply? Finally, we seek comment on whether complying with nonstructural safeguards such as special access performance metrics and imputation requirements adequately address issues of non-price discrimination and/or price squeezes. We ask commenters to provide detailed information on the overall costs and burdens of the section 64.1903 requirements on independent ILECs and their customers.

Paperwork Reduction Act

11. This NPRM seeks comment on a potential new or revised information collection requirement. If the Commission adopts any new or revised information collection requirement, the Commission will publish a separate notice in the Federal Register inviting the public to comment on the requirement, as required by the Paperwork Reduction Act of 1995, Public Law 104-13 (44 U.S.C. 3501-3520). In addition, pursuant to the Small Business Paperwork Relief Act of 2002, Public Law 107-198, see 44 U.S.C. 3506(c)(4), the Commission seeks specific comment on how it might “further reduce the information collection burden for small business concerns with fewer than 25 employees.”

Initial Regulatory Flexibility Analysis

12. As required by the Regulatory Flexibility Act of 1980, as amended (RFA), the Commission has prepared this Supplemental Initial Regulatory Flexibility Analysis (Supplemental IRFA) of the possible significant economic impact on a substantial number of small entities by the policies proposed in this Second NPRM. Written comments are requested on this Supplemental IRFA. Comments must be identified as responses to the Supplemental IRFA and must be filed by the deadlines for comments on the Second FNPRM. The Commission will send a copy of the Second FNPRM, including this Supplemental IRFA, to the Chief Counsel for

Advocacy of the Small Business Administration (SBA). In addition, the Second FNPRM and Supplemental IRFA (or summaries thereof) will be published in the Federal Register.

13. Purpose of the Proposed Rules. In the Second FNPRM, we explore the costs and benefits of continuing to apply the structural separation requirements contained in section 64.1903 of the Commission's rules, 47 CFR 64.1903, to independent incumbent local exchange carriers (ILECs) subject to rate-of-return regulation and providing in-region, interexchange, interstate long distance services (in-region long distance services) in today's marketplace.

14. In the Second FNPRM, we seek comments addressing marketplace changes such as the decline of stand-alone long distance services, the rise of facilities-based "all-distance services" competition from cable and wireless, and the role of bundles in today's long distance market. We therefore seek comment addressing whether incentives for anticompetitive behavior exist for independent ILECs subject to rate-of-return regulation, and whether granting relief from section 64.1903 is appropriate.

15. Legal Basis. The legal basis for any action that may be taken pursuant to the Second FNPRM is contained in sections 4(i), 4(j), 10, 201 through 204, 214, 220(a), and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. 154(i), 154(j), 160, 201 through 204, 214, 220(a), and 303(r).

16. Description and Estimate of the Number of Small Entities to Which the Proposed Rules Will Apply. RFA directs agencies to provide a description of and, where feasible, an estimate of the number of small entities that may be affected by the proposed rules, if adopted. The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction." In addition, the term "small business" has the same meaning as the term "small-business concern" under the Small Business Act. A small-business concern" is one which: (1) is independently owned and

operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the SBA.

17. Small Businesses. Nationwide, there are a total of approximately 27.5 million small businesses, according to the SBA.

18. Wired Telecommunications Carriers. The SBA has developed a small business size standard for Wired Telecommunications Carriers, which consists of all such companies having 1,500 or fewer employees. According to Census Bureau data for 2007, there were 3,188 firms in this category, total, that operated for the entire year. Of this total, 3144 firms had employment of 999 or fewer employees, and 44 firms had employment of 1000 employees or more. Thus, under this size standard, the majority of firms can be considered small.

19. Incumbent Local Exchange Carriers (ILECs). Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to incumbent local exchange services. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees. According to Commission data, 1,307 carriers reported that they were incumbent local exchange service providers. Of these 1,307 carriers, an estimated 1,006 have 1,500 or fewer employees and 301 have more than 1,500 employees. Consequently, the Commission estimates that most providers of incumbent local exchange service are small businesses that may be affected by rules adopted pursuant to the Second FNPRM.

20. We have included small incumbent LECs in this present RFA analysis. As noted above, a “small business” under the RFA is one that, inter alia, meets the pertinent small business size standard (e.g., a telephone communications business having 1,500 or fewer employees), and “is not dominant in its field of operation.” The SBA’s Office of Advocacy contends that, for RFA purposes, small incumbent LECs are not dominant in their field of operation because any such dominance is not “national” in scope. We have therefore included small incumbent LECs

in this RFA analysis, although we emphasize that this RFA action has no effect on Commission analyses and determinations in other, non-RFA contexts.

21. Interexchange Carriers (IXCs). Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to interexchange services. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees. According to Commission data, 359 companies reported that their primary telecommunications service activity was the provision of interexchange services. Of these 359 companies, an estimated 317 have 1,500 or fewer employees and 42 have more than 1,500 employees. Consequently, the Commission estimates that the majority of interexchange service providers are small entities that may be affected by rules adopted pursuant to the Order.

22. Description of Projected Reporting, Recordkeeping, and Other Compliance Requirements for Small Entities. In this Second FNPRM, the Commission proposes additional or modified information collections that would impose reporting and recordkeeping on current independent ILECs subject to rate-of-return regulation, including small entities. Specifically, the Second FNPRM invites comment on whether the Commission should replace its legacy framework for the provision of in-region, interstate long distance services provided by independent ILECs subject to rate-of-return regulation with a framework more closely tailored to the needs of consumers and competitors in today's marketplace. The central feature of this proposal is to amend or eliminate the application of section 64.1903 to independent ILECs subject to rate-of-return regulation.

23. Based on these questions, the Commission anticipates that a record will be developed concerning actual burdens and alternative ways in which the Commission could lessen the burdens on small entities subject to these requirements throughout the nation.

24. Steps Taken to Minimize the Significant Economic Impact on Small Entities, and Significant Alternatives Considered. The RFA requires an agency to describe any significant, specifically small business, alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): “(1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance and reporting requirements under the rules for such small entities; (3) the use of performance rather than design standards; and (4) an exemption from coverage of the rule, or any part thereof, for such small entities.”

25. The overall objective of this proceeding is to reduce regulatory burdens on independent ILECs to the extent consistent with the public interest, and is part of the Commission’s ongoing efforts under Executive Order 13,579 to revisit “rules that may be outmoded, ineffective, insufficient, or excessively burdensome, and to modify, streamline, expand, or repeal them in accordance with what has been learned.” The Second FNPRM seeks specific proposals as to which existing regulations might be removed or streamlined in their application to provision of in-region, interstate and international interexchange services by independent ILECs subject to rate-of-return regulation absent current safeguards, and asks parties to comment on whether such independent ILECs should continue to be classified as nondominant in the provision of such services if section 64.1903 is repealed. The Second FNPRM also asks parties to discuss whether, and to what extent, dominant carrier regulation is aptly suited to achieving the Commission’s objectives to promote competition and to deter anticompetitive behavior by independent ILECs subject to rate-of-return regulation. The Second FNPRM seeks comment on these matters, especially as they might affect small entities subject to the rules.

26. Federal Rules that May Duplicate, Overlap, or Conflict with the Proposed Rules.
None.

Ex Parte Presentations

27. This proceeding shall be treated as a “permit-but-disclose” proceeding in accordance with the Commission's ex parte rules. Persons making ex parte presentations must file a copy of any written presentation or a memorandum summarizing any oral presentation within two business days after the presentation (unless a different deadline applicable to the Sunshine period applies). Persons making oral ex parte presentations are reminded that memoranda summarizing the presentation must (1) list all persons attending or otherwise participating in the meeting at which the ex parte presentation was made, and (2) summarize all data presented and arguments made during the presentation. If the presentation consisted in whole or in part of the presentation of data or arguments already reflected in the presenter’s written comments, memoranda or other filings in the proceeding, the presenter may provide citations to such data or arguments in his or her prior comments, memoranda, or other filings (specifying the relevant page and/or paragraph numbers where such data or arguments can be found) in lieu of summarizing them in the memorandum. Documents shown or given to Commission staff during ex parte meetings are deemed to be written ex parte presentations and must be filed consistent with section 1.1206(b). In proceedings governed by section 1.49(f) or for which the Commission has made available a method of electronic filing, written ex parte presentations and memoranda summarizing oral ex parte presentations, and all attachments thereto, must be filed through the electronic comment filing system available for that proceeding, and must be filed in their native format (e.g., .doc, .xml, .ppt, searchable .pdf). Participants in this proceeding should familiarize themselves with the Commission’s ex parte rules.

Ordering Clauses

28. Accordingly, IT IS ORDERED that, pursuant to Sections 1, 2, 4(i), 4(j), 201 through 205, 220(a), 251, 272, and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. 151, 152, 154(i), 154(j), 201 through 205, 220(a), 251, 272, and 303(r) this Second Further

Notice of Proposed of Rulemaking in CC Docket No. 00-175 IS ADOPTED.

29. IT IS FURTHER ORDERED that the Commission's Consumer and Governmental Affairs Bureau, Reference Information Center, SHALL SEND a copy of this Second Further Notice of Proposed Rulemaking in CC Docket No. 00-175, including the Initial Regulatory Flexibility Certifications, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION.

Marlene H. Dortch,
Secretary.

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